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tion for a rehearing was filed August 10, 1933 (R 143–146), and was denied October 10, 1933 (R. 151). The petition for a writ of certiorari was filed November 10, 1933. The jurisdiction of this Court is invoked under Section 240 (a) of the Judicial Code, as amended by the Act of February 13, 1925.

QUESTION PRESENTED

The petitioner was affiliated with two subsidiary corporations by the ownership of all of such corporations' stock during the year 1929 and for some years prior thereto. During the year 1929, up to and including the month of November, 1929, the subsidiary corporations liquidated and sold all of their assets to outside interests and in December, 1929, turned over to the petitioner the cash proceeds realized from liquidation. Such cash proceeds were less in amount in each case than the cost of the subsidiary's stock to the petitioner, plus advances theretofore made by the petitioner to the subsidiary. During the period of affiliation the petitioner was enabled through the medium of consolidated returns to deduct from its income losses of the subsidiaries exceeding in amount the difference between the cost of the stock plus advances made and the amounts received on liquidation. Was the petitioner entitled to deduct any amounts from its income for 1929 as a result of the liquidation of the subsidiaries?

STATUTE AND REGULATIONS INVOLVED

The applicable provisions of the statute and regulations involved will be found in the Appendix, *infra*, pp. 12–19.

STATEMENT

Petitioner brought this suit in the District Court for New Mexico for the recovery of income taxes paid for the year 1929. (R. 1–5.) Jury trial was waived in writing (R. 12) and the court made findings of fact and conclusions of law (R. 20–25). The findings may be summarized as follows:

The petitioner purchased all of the capital stock of the Springer Trading Company in 1917 and all of the capital stock of the Roy Trading Company in 1920 and operated both corporations as affiliated or subsidiary corporations from the dates of such purchases up to and including the month of November, 1929. During the years of such operation the petitioner filed affiliated returns and availed itself of the annual operating losses of the subsidiaries during the period of affiliation. (R. 20–21.)

The petitioner paid the sum of $40,000 for the Springer Trading Company stock and during the period from 1917 to 1929 advanced and loaned to the latter company the sum of $69,030.27. During the year 1929, up to and including the month of November, the Springer Trading Company liquidated and sold all of its assets to outside interests and paid off its obligations. In December, 1929, the Springer Trading Company turned over to the petitioner the cash proceeds derived from liquida-

tion in the sum of $22,914.22. The petitioner sustained a loss on its capital investment in the Springer Trading Company in the sum of $86,116.05, which was charged off the petitioner's books as a loss at the close of the year 1929. (R. 21.)

The petitioner paid the sum of $50,000 for the Roy Trading Company stock and during the period from 1920 to 1929 advanced and loaned the latter company the sum of $9,782.22. During the year 1929, up to and including the month of November, the Roy Trading Company liquidated and sold all of its assets to outside interests and paid all of its obligations. In December, 1929, the Roy Trading Company turned over to the petitioner the cash proceeds derived from liquidation in the sum of $15,106.16. The petitioner sustained a loss on its capital investment in the Roy Trading Company in the sum of $44,676.06 which was charged off the petitioner's books as a loss at the close of the year 1929. (R. 21–22.)

Both the Springer Trading Company and the Roy Trading Company were liquidated and dissolved in the month of November, 1929.[1] (R. 22.)

In the year 1930, the petitioner filed its consolidated return covering its operations and those of

[1] The finding that the two corporations were dissolved in November, 1929, is not sustained by the record. It does appear that the stock of both corporations was voted at stockholders meetings held on December 30, 1929, and that dissolution occurred on that date (R. 56–57). And see Record pp. 89, 135. This finding was assigned as error. (R. 126.)

the Roy Trading Company and the Springer Trading Company, without deducting the losses sustained by it on the liquidation and dissolution of the two subsidiaries, and paid to the Collector the sum of $20,836.20 in equal quarterly installments. (R. 22–23.) Thereafter, in May, 1931, the petitioner filed an amended return and claim for refund for the year 1929 setting up these losses as deductible. (R. 23.) The claim for refund was rejected by the Commissioner on January 28, 1932. (R. 23.)

The petitioner has claimed and been allowed, in the aggregate, as deductions from its own net income for the taxable years 1918 to 1928, inclusive, the total sum of $131,424.41, and charged with and taxed upon profits in the total sum of $12,913.88, or allowed aggregate net deductions from its own taxable net income of $118,510.53 on account of operating losses sustained by the Springer Trading Company. (R. 24.)

The petitioner has claimed and been allowed, in the aggregate, as deductions from its own net income for the taxable years from 1920 to 1929, inclusive, the total sum of $61,535.17, and charged with and taxed upon the profits in the total sum of $4,407.32, or allowed aggregate net deductions from its own taxable net income of $58,127.85 on account of operating losses sustained by the Roy Trading Company. (R. 24.)

The District Court rendered judgment for the petitioner in the sum of $14,460.43, with interest. (R. 25–26, 122–123.) The Circuit Court of Ap-

If, as the court below held, the case is one in which the parent's loss suffered in liquidation of the subsidiaries was recognizable, nevertheless as the court also held, the regulations do not contemplate that the petitioner was entitled to deduct its investment twice. Since, through the medium of consolidated returns in prior years, the petitioner had exercised the right to offset against its income losses of the subsidiaries exceeding in amount the capital loss now claimed, no deduction should be allowable for the year 1929. In promulgating Article 34 (*c*) (2) of Regulations 75 (*infra*, pp. 14, 15), upon which the petitioner relies, the Commissioner was evidently prescribing rules only with respect to 1929 and subsequent years. We do not believe either the statute or the regulations contemplated that a double deduction should be permitted where the losses occurred in years prior to 1929 when such deductions were denied in the case of losses occurring in 1929 and subsequent years. As the court below stated (R. 148), this would be an unjust and anomalous result not lightly to be attributed to the Treasury Department.

But if such is the result of the regulations, nevertheless we submit that the decision of the court below does not result in prejudicial error. While the court held that the capital loss was recognizable, we believe that its determination in this respect was contrary to the provisions of the regulations. In other words, since the record shows that on

December 30, 1929, the petitioner owned and voted the stock of its subsidiaries and certificates of suspension of business had not been filed by the subsidiaries prior to that date (R. 56–57), it is apparent that in November, 1929, when the distributions were made affiliation still existed between the petitioner and the liquidating corporations. Cf. *Barnet* v. *Aluminum Goods Co.*, 287 U.S. 544. Consequently, the distributions occurred during a consolidated return period and Articles 37 (a) and 40 (a) of Regulations 75 (*infra*, pp. 18, 19), are applicable. Under these provisions no gain or loss is recognizable since the transactions are considered intercompany in their nature.

We do not believe there is a direct conflict between the decision of the court below and those in the cases cited by the petitioner. (Br. 8–11.) All of those cases were decided under revenue acts prior to the Revenue Act of 1928. The decision below, as evidenced by the opinion denying the petition for rehearing, is predicated on the effect of Regulations 75 promulgated under the Revenue Act of 1928, legislative in character, and in this respect differing from those under prior acts. As the petitioner states (Br. 17), this is the first case presented to this Court for an interpretation of the 1928 Act and the rules promulgated thereunder touching consolidated returns. Consequently, a decision here would not necessarily resolve any conflicts existing under the provisions of the earlier acts.

If the question presented is the same under the Revenue Act of 1928 and Regulations 75 as under prior acts, nevertheless we believe the only decision directly in conflict is that of the District Court for the Southern District of New York in *United Publishers' Corp.* v. *Anderson,* 42 F. (2d) 781. In *McLaughlin* v. *Pacific Lumber Co.,* 66 F. (2d) 895 (C.C.A. 9th), the court did not specifically hold that prior years' losses taken as deductions by the parent should not be offset against a loss on liquidation, but stated that the collector had failed to establish any specific instance of a double deduction. While in *Burnet* v. *Imperial Elevator Co.,* 66 F. (2d) 643 (C.C.A. 8th), the court stated that operating losses of the subsidiary are different from losses on its stock, the court also pointed out that the stock loss suffered by the parent corporation for the fiscal year 1923 was more than sufficient to offset its income both for 1923 and 1925 and it was, therefore, immaterial whether an operating loss or a part of the capital loss was applied in 1923 against the petitioner's income. Two other Circuit Courts of Appeals have held under the law prior to the 1928 Act that losses deducted by the parent for prior years must be offset against a final capital loss. Cf. *Burnet* v. *Riggs Nat. Bank,* 57 F. (2d) 980 (C.C.A. 4th); *Commissioner* v. *Apartment Corp.,* 67 F. (2d) 3 (C.C.A. 4th). The same principle was suggested by this Court, although not necessary for the decision, in the case of *Burnet* v. *Aluminum Goods Co., supra.*

CONCLUSION

While the questions presented are probably important as an administrative matter for prior years as well as for the year 1929 and subsequent years, nevertheless in the absence of a direct conflict between the decision here and those in other Circuit Courts of Appeals, and because we believe the decision below is correct, we oppose the petition in this case.

Respectfully submitted.

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DECEMBER, 1933.

APPENDIX

REVENUE ACT OF 1928, C. 852, 45 STAT. 791, 822, 831

SEC. 115. DISTRIBUTIONS BY CORPORATIONS.

* * * * * *

(c) *Distributions in liquidation.*—Amounts distributed in complete liquidation of a corporation shall be treated as in full payment in exchange for the stock, and amounts distributed in partial liquidation of a corporation shall be treated as in part or full payment in exchange for the stock. The gain or loss to the distributee resulting from such exchange shall be determined under section 111, but shall be recognized only to the extent provided in section 112. In the case of amounts distributed in partial liquidation (other than a distribution within the provisions of section 112 (h) of stock or securities in connection with a reorganization) the part of such distribution which is properly chargeable to capital account shall not be considered a distribution of earnings or profits within the meaning of subsection (b) of this section for the purpose of determining the taxability of subsequent distributions by the corporation.

SEC. 141. CONSOLIDATED RETURNS OF CORPORATIONS—1929 AND SUBSEQUENT TAXABLE YEARS.

(a) *Privilege to file consolidated returns.*—An affiliated group of corporations shall, subject to the provisions of this section, have the privilege of making a consolidated return for the taxable year

1929 or any subsequent taxable year, in lieu of separate returns. The making of a consolidated return shall be upon the condition that all the corporations which have been members of the affiliated group at any time during the taxable year for which the return is made consent to all the regulations under subsection (b) prescribed prior to the making of such return; and the making of a consolidated return shall be considered as such consent. In the case of a corporation which is a member of the affiliated group for a fractional part of the year the consolidated return shall include the income of such corporation for such part of the year as it is a member of the affiliated group.

(b) *Regulations.*—The Commissioner, with the approval of the Secretary, shall prescribe such regulations as he may deem necessary in order that the tax liability of an affiliated group of corporations making a consolidated return and of each corporation in the group, both during and after the period of affiliation, may be determined, computed, assessed, collected, and adjusted in such manner as clearly to reflect the income and to prevent avoidance of tax liability.

(c) *Computation and payment of tax.*—In any case in which a consolidated return is made the tax shall be determined, computed, assessed, collected, and adjusted in accordance with the regulations under subsection (b) prescribed prior to the date on which such return is made. Only one specific credit, computed as provided in section 26 (b), shall be allowed in computing the tax.

TREASURY REGULATIONS 75, PROMULGATED UNDER THE REVENUE ACT OF 1928

APPLICATION OF REGULATIONS

(a) *1929 and Subsequent Years.*

These regulations are applicable only to the taxable year 1929 and to subsequent taxable years.

ART. 2.—*Definitions.*

* * * * *

(c) *Consolidated Return Period.*

The term "consolidated return period" means the taxable year 1929, or any subsequent taxable year, for which a consolidated return is made or is required.

ART. 34.—*Sale of Stock—Basis for determining Gain or Loss.*

(a) *Scope of Article.*

This article prescribes the basis for determining the gain or loss upon any sale or other disposition (hereinafter referred to as "sale") by a corporation which is (or has been) a member of an affiliated group which makes (or has made) a consolidated return for the taxable year 1929 or any subsequent taxable year, of any share of stock issued by another member of such group (whether issued before or during the period that it was a member of the group and whether issued before, during, or after the taxable year 1929), and held by the selling corporation during any part of a consolidated return period. (For the basis in the case of sales of bonds, see article 35.) The paragraphs of this article are applicable to sales during different periods of time, as follows:

(1) Sales which do not break the affiliation—paragraph (b);

(2) Sales which break the affiliation and which are made during the period that the selling corporation is a member of the affiliated group (whether or not during a consolidated return period)—paragraph (c);

(3) Sales made after the selling corporation has ceased to be a member of the affiliated group—paragraph (d).

(b) *Sales which do not Break Affiliation.*

If notwithstanding any such sale the issuing corporation remains a member of the affiliated group, such basis shall be determined and adjusted in the same manner as if the selling corporation and the issuing corporation had never been members of an affiliated group. (See sections 111 to 115, inclusive, of the Act, and articles 561 to 629, inclusive, of Regulations 74.)

(c) *Sales which break Affiliation made while Selling Corporation is Member of Group.*

If the sale is made during a period which the selling corporation is a member of the affiliated group (whether or not during a consolidated return period), and if, as a result of such sale, the issuing corporation ceases to be a member of the affiliated group, such basis shall be determined as follows:

(1) The aggregate basis of all shares of stock of the issuing corporation held by each member of the group (exclusive of the issuing corporation) immediately prior to the sale, shall be determined separately for each member of the group, and adjusted in accordance with the Act (see sections 111 to 115, inclusive, of the Act, and articles 561 to 629, inclusive, of Regulations 74);

(2) From the sum of the aggregate bases, as determined in paragraph (1) above, there shall be

deducted the aggregate of the losses of such issuing corporation sustained during each of the consolidated return periods (including only the taxable year 1929 and subsequent taxable years) after such corporation became a member of the group and prior to the sale of the stock, to the extent that such losses could not have been availed of by such corporation as a net loss in computing its tax for such periods if it had made a separate return for each of such periods;

(3) The total aggregate basis of all shares of stock, after making the deduction under paragraph (2), shall then be allocated to each member of the group which holds stock in the issuing corporation, in the ratio that the basis of each, as determined under paragraph (1), is to the sum of the bases of all;

(4) The aggregate basis as determined under paragraph (3) for each member of the group shall then be equitably apportioned among the various classes of stock held by such member, according to the circumstances of the case—ordinarily in the ratio that the basis of each class of stock held by it at the time of the sale is to the sum of the bases of each class of stock held by it;

(5) The basis of each share of stock of each class held by a member of the group shall then be determined by dividing the basis apportioned to such class under paragraph (4) by the total number of shares of such class held by it.

* * * * *

(d) *Sales after Selling Corporation has ceased to be a Member of the Group.*

If the sale is made after the selling corporation has ceased to be a member of the affiliated group,

such basis shall be determined in accordance with paragraph (c) of this article, except that—

(1) The aggregate basis (under subparagraph (1) of such paragraph) shall be determined for all shares of the issuing corporation held by each member of the group immediately prior to the time the selling corporation ceased to be a member of the group (rather than immediately prior to the sale); and

(2) The allocations (under subparagraph (3) of such article) shall be made to each member of the group which held stock of the issuing corporation immediately prior to the time the selling corporation ceased to be a member of the group (rather than to the members holding such stock at the time of the sale); and

(3) The basis of each share of stock held by the selling corporation (determined, as above, as of the time the selling corporation ceased to be a member of the group) shall then be adjusted in accordance with the Act (see, particularly, sections 111 to 115, inclusive, of the Act and articles 561 to 629, inclusive, of Regulations 74) in order to determine the basis at the time of the sale.

(e) *Limitation on Adjustment For Losses.*

No deduction shall be made under paragraph (c) (2) of this article, in the event of a consolidated net loss which was sustained more than two years prior to the close of the taxable year during which the sale was made and which was not availed of by the members of the affiliated group in computing the tax for the consolidated return period, for that portion of such net loss which the losses of the subsidiary for the year in which such net loss was sus-

tained bears to the aggregate losses of each of the members of the group.

* * * * *

ART. 35.—*Sale of Bonds—Basis for determining Gain or Loss.*

In the case of a sale or other disposition by a corporation, which is (or has been) a member of an affiliated group which makes (or has made) a consolidated return for the taxable year 1929 or any subsequent taxable year, of bonds issued by another member of such group (whether or not issued while it was a member of the group and whether issued before, during, or after the taxable year 1929), the basis of each bond, for determining the gain or loss upon such sale or other disposition, shall be determined in accordance with the Act (see, particularly, section 113 of the Act), but the amount of any loss otherwise allowable shall be decreased by the excess (if any) of the aggregate of the deductions computed under paragraph (c) (2) of Article 34 over the aggregate of the basis of the stock of the issuing corporation as computed under paragraph (c) (1) or (d), as the case may be, held by the members of the affiliated group. (See, also, Article 40 (c), relating to disallowance of loss upon intercompany bad debts.)

ART. 37.—*Dissolutions—Recognition of Gain or Loss.*

(a) *During Consolidated Return Period.*

Gain or loss shall not be recognized upon a distribution during a consolidated return period, by a member of an affiliated group to another member of such group, in cancellation or redemption of all or any portion of its stock; and any such distribution shall be considered an intercompany transaction.

(b) *After Consolidated Return Period.*

Any such distribution after a consolidated return period, whether in complete or partial liquidation, shall be treated as a sale of the stock, and the adjustments specified in articles 34 and 35 will be made, and article 36 will be applicable.

ART. 40.—*Bad Debts.*

(a) *Resulting From Transactions During Consolidated Return Period.*

Intercompany accounts receivable or other obligations which are the result of intercompany transactions during a consolidated return period shall not be deducted as bad debts during a consolidated return period.

* * * * *

(e) *Limitation on Allowance after Consolidated Return Period.*

The rules applicable to the allowance of losses upon the sale of bonds shall be applicable to the allowance after the consolidated return period as a bad debt of an intercompany account receivable or other obligation resulting from an intercompany transaction during the consolidated return period. (See article 35.)

U. S. GOVERNMENT PRINTING OFFICE: 1933